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COMMISSIONERS

Mike Gleason, Chairman
 William A. Mundell
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BEFORE THE ARIZONA CORPORATION COMMISSION

ARIZONA WATER COMPANY, an Arizona
 corporation,

Complainant,

vs.

GLOBAL WATER RESOURCES, LLC, a
 foreign limited liability company; GLOBAL
 WATER RESOURCES, INC., a Delaware
 corporation; GLOBAL WATER
 MANAGEMENT, LLC, a foreign limited
 liability company; SANTA CRUZ WATER
 COMPANY, LLC, an Arizona limited liability
 corporation; PALO VERDE UTILITIES
 COMPANY, LLC, an Arizona limited liability
 corporation; GLOBAL WATER - SANTA
 CRUZ WATER COMPANY, an Arizona
 corporation; GLOBAL WATER - PALO
 VERDE UTILITIES COMPANY, an Arizona
 corporation; JOHN AND JANE DOES 1-20;
 ABC ENTITIES I - XX,

Respondents.

DOCKET NOS.

W-01445A-06-0200

SW-20445A-06-0200

W-20446A-06-0200

W-03576A-06-0200

SW-03575A-06-0200

**PRE-FILED DIRECT TESTIMONY
 OF JOSEPH D. HARRIS ON
 BEHALF OF ARIZONA WATER
 COMPANY**

Arizona Corporation Commission

DOCKETED

AUG 03 2007

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ARIZONA CORPORATION COMMISSION
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2 **Q. WHAT IS YOUR NAME, EMPLOYER AND OCCUPATION?**

3 A. My name is Joseph D. Harris. I am employed by Arizona Water Company as Vice
4 President and Treasurer.
5

6
7 **Q. PLEASE DESCRIBE YOUR WORK EXPERIENCE AND EDUCATIONAL**
8 **BACKGROUND.**

9 A. I have been Vice President and Treasurer of Arizona Water Company since March
10 2007. I received a Bachelor of Science degree in Accounting from Eastern Illinois
11 University in 1981 and am a Certified Public Accountant in the State of Illinois. From
12 approximately 1982 until 1999, I worked for Northern Illinois Water Company, first as Staff
13 Accountant and (from 1986 to 1999) as Chief Accountant, where I managed the accounting
14 department and oversaw the company's financial reporting, tax compliance, strategic
15 planning and filings with the Illinois Commerce Commission. From November 1999 until
16 July 2002, I served as Comptroller of Illinois American Water Company, managing the
17 company's accounting and information system departments. From July 2002 until March
18 2007, I worked for American Water Service Company, first as Senior Financial Analyst and
19 later as Manager for Performance, Planning and Reporting, where I directed and
20 coordinated preparation of the company's annual business plan and quarterly forecasts and
21 provided financial expertise on all financial issues affecting the company. I am also a
22 member of the American Institute of Certified Public Accountants.
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1
2 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

3 **A.** The purpose of my testimony is to evaluate the aberrant service model employed by
4 Respondents (collectively, "Global"), which relies upon unconventional agreements, called
5 Infrastructure Coordination and Financing Agreements ("ICFAs"), between the unregulated
6 Global Water Resources, LLC ("GWR") and developers, by which the developers are
7 required to make extensive payments to GWR and which payments GWR then uses to fund
8 its regulated subsidiaries, Santa Cruz Water Company ("SCWC") and Palo Verde Utility
9 Company ("PVUC"), outside of the scrutiny of the Commission. Global's service model
10 also includes Public Private Partnerships ("P3 Agreements") involving the municipalities of
11 Casa Grande and Maricopa, under which Global pays the municipalities some portion of the
12 monies Global collected from landowners and developers under the ICFAs in exchange for
13 the municipalities' support in Global's regulated subsidiaries' CCN extension requests.
14
15

16
17 Global also uses an unconventional service model under which Global's regulated
18 subsidiaries actually have no employees but instead rely upon an unregulated Global
19 affiliate, Global Water Management, LLC ("GWM"), to provide contract services, for
20 which GWM charges alleged "market rates." These payments for contract services are also
21 not subject to Commission scrutiny, thus potentially allowing Global to receive additional
22 unregulated profits at the expense of the regulated subsidiaries.
23

24 All of these schemes have resulted in a situation in which Global's regulated
25 subsidiaries have been able, according to Global's public filings with the Commission, to
26 enjoy extremely favorable rates of return, perhaps as much as 28% return on rate base, on
27
28

1 questionable equity. Moreover, this only reflects the disclosed rate of return of Global's
2 regulated subsidiaries, and does not indicate the undisclosed profits that GWR, GWM and
3 other unregulated affiliates have been able to receive from the ICFA's and the other inter-
4 company payments.
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8 **Q. WILL YOU BE SPONSORING ANY EXHIBITS WITH YOUR DIRECT**
9 **TESTIMONY?**
10

11 A. Yes. I will be sponsoring the following exhibits:

12 JDH-1: Global's Expectation of ICFA Fee Revenues

13 JDH-2: Global's Organizational Chart

14 JDH-3: Arizona Water Company's Data Request 1.93

15 JDH-4: Global's Response to Staff's Data Request LJ 1.1
16
17

18 **Q. ARE YOU FAMILIAR WITH ARIZONA WATER COMPANY'S ATTEMPT**
19 **TO GATHER FINANCIAL DATA AND INFORMATION FROM GLOBAL?**
20

21 A. Yes, I am.
22

23 **Q. PLEASE REPORT ON THE STATUS OF ARIZONA WATER COMPANY'S**
24 **ATTEMPT TO GATHER SUCH INFORMATION FROM GLOBAL?**
25

26 A. In Docket No. W-01445A-06-0199, which discovery the parties have stipulated may
27 be used in this Docket, Arizona Water Company served a number of data requests aimed at
28

1 uncovering the details and workings of Global's financial arrangements, particularly the
2 ICFAs, the P3 Agreements and Global's inter-company agreements and payments for
3 services. Specifically, Arizona Water Company submitted data requests AWC 1.100 and
4 AWC 1.102 to Global, seeking financial information concerning the inter-company dealings
5 of PVUC, GWR, GWM or any other affiliated Global entity. Legal Counsel for Global
6 provided the same response to both: "Objection. This request seeks information that is
7 overly broad, unduly burdensome, irrelevant and not reasonably calculated to lead to the
8 discovery of any admissible evidence. Further, the information sought is proprietary
9 business information that is confidential."
10
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13 Global's disclosure of information and documents has been grudging at best. While
14 Global has provided some information related to SCWC and PVUC, Global has routinely
15 and consistently refused to provide any information about the finances of GWR, GWM or
16 other unregulated Global affiliates, thus preventing a full understanding of Global's
17 operations and finances.
18

19 For example, I participated in a series of meetings at Global's offices over the past
20 several weeks regarding Arizona Water Company's data requests seeking this information.
21 Global allowed representatives of Arizona Water Company to review only the general
22 ledger of SCWC for the years 2004, 2005 and 2006, while maintaining its objections to
23 disclosure of the lion's share of information that Arizona Water Company was seeking..
24 Arizona Water Company's limited inspection of SCWC's ledgers revealed that SCWC has
25 used its capital stock account as an inter-company cash balance account, with funds coming
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1 in from both outside sources such as customer payments and from GWR. However,
2
3 because GWR has provided no financial information, Arizona Water Company was unable
4 to determine the source of the funds coming from GWR, particularly as to the extent to
5 which those funds are derived from ICFAs. Similarly, because Global refused to provide
6 financial information related to GWR, Arizona Water Company was unable to determine
7 the extent of any payments to municipalities under P3 Agreements, and how those funds
8 may have been traced through the regulated subsidiaries.
9

10 Concerning the ICFAs, again, Global has provided only cryptic and incomplete
11 information. Following Arizona Water Company's initial data requests, Global provided an
12 illegible and confusing list of what seemed to be more than 200 ICFAs. In May 2007, seven
13 months after Arizona Water Company first requested information about the ICFAs, Global
14 produced a CD containing 129 ICFAs, which Global averred were "all" of the ICFAs.
15 Arizona Water Company through its own efforts knew of other ICFAs and brought that fact
16 to Global's attention. In a letter dated July 23, 2007, Global produced yet another list of
17 "all" ICFAs, which listed 151 ICFAs. The lists are inconsistent and confusing. As of this
18 date, Arizona Water Company still does not know exactly how many ICFAs Global has
19 entered into, let alone the financial impact of those ICFAs.
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23 Global has generally refused to identify and account for the fees it has received under
24 the ICFAs. (See Global's response to Arizona Water Company's data request AWC 1.101.)
25 However, in its July 23, 2007 letter, Global produced a chart allegedly estimating the "total
26 fees expected from ICFAs" within Global's requested extension area in Docket No. W-
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1 01445A-06-0199. That chart is Exhibit JDH-1 to my testimony. Concerning the 50 ICFAs
2 listed on that chart, Global estimated that it would receive more than **\$312 million** in fees.
3 (As noted above, this amount does not reflect the total in ICFA fees, only the total in that
4 particular extension area.) If developers paid this amount to a regulated utility such as
5 SCWC, the funds would have to be recorded as advances or contributions in aid of
6 construction, not in the equity account. However, Global apparently is attempting to shield
7 these funds from Commission inquiry by having them paid to GWR rather than SCWC.
8

9
10 Arizona Water Company has also been unable to determine from the information
11 provided by Global exactly how the payments collected by GWR under the ICFAs are
12 calculated. Each ICFA requires a payment per Equivalent Dwelling Unit ("EDU"), but the
13 payment amount varies widely from one ICFA to another. Although Trevor Hill
14 characterized the amount as an "interest carry," he was unable to explain how the amount
15 was calculated. Hill Depo. at 55-56, 78-80. Similarly, Cynthia Liles, who Global
16 designated to speak on ICFA topics, was unable to explain how the payment amount was
17 calculated. Liles Depo. at 44-46.
18

19
20 Global has also refused to respond to data requests on Global's sources of equity
21 (AWC 1.50, 1.51, 1.52 and 1.102), so Arizona Water Company has generally been unable to
22 trace Global's potential use of ICFA funds as a source of equity for GWR and ultimately its
23 subsidiaries SCWC and PVUC. Instead, Global's witnesses have only admitted that the
24 ICFA funds go into GWR's general revenues, and are then disbursed to its subsidiaries.
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1 Liles Depo. at 47-56. However, Arizona Water Company has been frustrated in its attempts
2 to trace particular funds from an ICFA to their ultimate use.
3
4

5 **Q. WHAT HAS ARIZONA WATER COMPANY BEEN ABLE TO DETERMINE**
6 **ABOUT THE OPERATION AND FUNCTION OF GLOBAL'S ICFAS?**
7

8 **A.** Global's ICFAs are an unorthodox type of financing agreement between a non-
9 regulated Global affiliate and developers that distorts the regulated Global utilities' capital
10 structure by understating and obscuring the correct amount of advances and contributions
11 provided by developers that should be deducted from (instead of being added to) rate base
12 and overstating the amount of common equity on which the regulated utilities are entitled to
13 earn a return.
14

15 Global's non-regulated affiliates not only execute such non-traditional financing
16 arrangements with landowners and developers for the provision of utility services, they also
17 refuse to explain their accounting for the payments received under these arrangements.
18

19 As discussed more fully in the Commission's own proceeding *Evaluation of the*
20 *Regulatory Impact from the Use of Non-Traditional Financing Arrangements by Water*
21 *Utilities and Their Affiliates*, Docket No. W-00000C-06-0149 ("Generic Docket") and the
22 Staff Report thereto, Global has developed and implemented unorthodox long-term
23 financing agreements, all without Commission approval. The ICFA's are somewhat similar
24 in effect but are more complex than the earlier PILOR agreements (payments in lieu of
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1 revenue) attempted by SCWC and PVUC, and rejected by the Commission. (Decision No.
2 61943, September 17, 1999).

3
4 Depositions of Global's representatives also failed to provide any illumination
5 on the flow of ICFA funds into GWR and GWR's use of those funds, including the
6 provision of funding to its regulated subsidiaries, SCWC and PVUC. See Liles Depo. at 46-
7 67. While Global seemed to admit that the ICFA funds went into Global's general fund and
8 were not specifically earmarked for a particular developer or development, Global also
9 seemed to contend that none of the ICFA funds (which Global characterized as an "interest
10 carry") were ever used by the regulated subsidiaries to fund infrastructure. *Id.* at 56. Global
11 also conceded that none of these transfers of equity or retained earnings or whatever
12 between GWR and its subsidiaries were documented by promissory notes, but were instead
13 treated as "capital infusions." *Id.* at 57-58. While Global's representatives made numerous
14 assertions as to what the ICFA funds were *not* used for, Global was incapable of explaining
15 what the ICFA funds were used for, other than the acquisition of other utilities. Hill Depo.
16 At 82-83.

17
18 The ICFAs, like the PILORs, bypass the customer protections embodied in the
19 Commission's Main Extension Rule, R14-2-406. An unregulated Global affiliate, GWR,
20 has executed ICFAs covering utility services for approximately 170,000 units in the SCWC
21 and PVUC service area as of September 2006. However, no one outside of Global knows:

- 22 • The status of these agreements
 - 23 • How much money has been collected
- 24
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- How much additional money will be collected
- What contractual obligations the ICFAs place on the regulated utilities
- What accounting procedures have been followed
- How the money collected is supposed to be used
- How the money collected has actually been used
- How much of the regulated subsidiaries' equity capital is derived from

ICFA payments

Although in the Generic Docket, Staff concluded that ICFAs should be treated as advances or contributions, instead of equity, the Staff Report did not address any of the above questions. Staff conducted no independent investigation and did not recommend any remedial action by the Commission to forestall ICFA funds from being added to the regulated utilities equity. Moreover, the Staff Report did not address the broader jurisdictional issues about whether the non-regulated affiliates entering into ICFAs should be considered public service corporations subject to Commission audits and regulation.

If Global's ICFA procedure is allowed to continue and cover new CCN extension areas, evaluating SCWC's future rate filings will be extraordinarily complex, if not impossible, and time intensive. The Commission should not endorse the continuation and expansion of the now-discredited Algonquin Water Resources of America ("AWRA") model as further complicated by Global. Global's aberrant operating and financing model is designed to benefit its shareholders at the expense of the customers of its regulated utility subsidiaries. Allowing Global's service territories to be enlarged in light of its questionable

1 and likely unlawful operating, financing and accounting practices irreparably harms the
2 public interest.
3

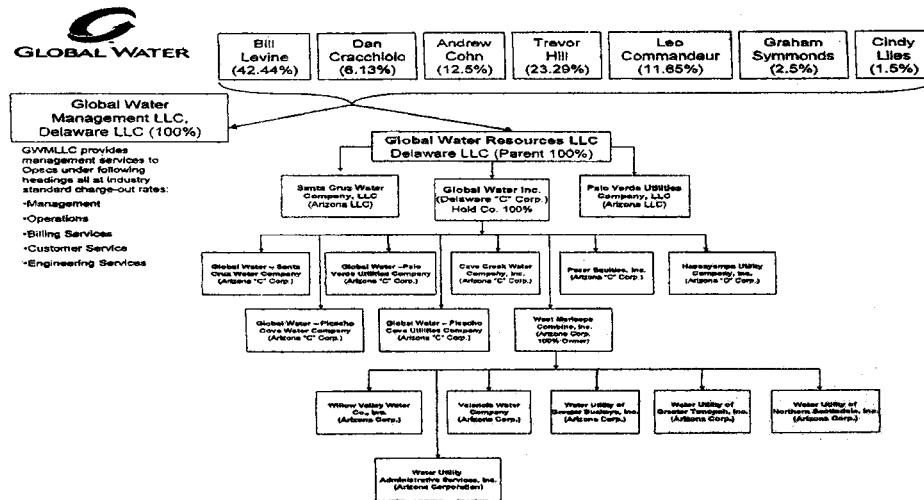
4
5 **Q. WHY SHOULD THE COMMISSION BE CONCERNED ABOUT GLOBAL'S**
6 **RELATIVE RATES AND THE EFFECT GLOBAL'S BUSINESS MODEL MAY**
7 **HAVE ON THOSE RATES?**
8

9 **A.** As stated by the Arizona Supreme Court in the *James P. Paul* case: "The public
10 interest is the controlling factor in decisions concerning the service of water by water
11 companies." In addition to the qualifications and capabilities of competing utilities, as
12 discussed in Mr. Garfield's testimony, the customers' ultimate expense is a primary
13 determinant of the public interest.
14

15
16 **Q. DO YOU BELIEVE THAT SCWC IS LESS EFFICIENT THAN ITS**
17 **ARIZONA PEERS?**
18

19 **A.** Yes, but the true answer lies in the complexity of Global's corporate structure, the
20 way employee services are provided, marked up, and charged to Global's regulated utilities
21 by its unregulated affiliates, and Global's incomplete and unsubstantiated responses to
22 discovery requests from Arizona Water Company. The various Global entities affiliated
23 with its regulated water and sewer utilities form an unconventional and unusually complex
24 structure, illustrated on the following chart and Exhibit JDH-2, which Global provided to
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Arizona Water Company and Staff in response to a Staff data request (a larger version is in the exhibit itself):



Since SCWC has no employees, all utility work including management, operations, billing, customer service and engineering, is provided to SCWC and the other wholly owned operating utilities by the left-most entity on the organization chart, the unregulated GWM, through various layers of the organization. As stated by Trevor Hill in his deposition, it is part of Global's business plan that none of the regulated utilities would actually have any employees, instead relying upon unregulated affiliates to provide services. Hill Depo. at 37.

1 GWM charges the regulated utilities "market based prices" (that is, it marks up the
2 actual costs with additional profit margin, as the "market" would) for this work, which in
3 almost all other utilities is performed by utility employees at actual cost. In other words, the
4 inter-company charges are not limited to the cost of the workers' wages and benefits, as is
5 the case of almost every other regulated Arizona utility; instead GWM determines are
6 appropriate prices and then passes on to the regulated affiliate without a contract.
7

8
9 Global has refused to provide information about these costs, other than to contend
10 summarily that there was no profit component in the prices charged by GWM to SCWC and
11 PVUC. Hill Depo. at 38. However, Global has failed to provide sufficient information that
12 would enable an interested analyst—or the Commission—to determine the reasonableness
13 of these charges to SCWC, PVUC and their other captive operating utilities, how often they
14 are charged or the amount of profit added to the actual costs as they are passed through by
15 the various affiliates on their way to the regulated utilities. Trevor Hill also admitted in his
16 deposition that no written contract existed for these services, and that GWM simply renders
17 a bill to SCWC and PVUC, which the captive subsidiaries then pay without discussion or
18 further negotiation. Hill Depo. at 72-73.
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22 AWC Data Request 1.93, which appears as Exhibit JDH-3, sought to obtain the total
23 costs of each common or shared service and for each service the amount and percentage of
24 the total costs allocated to each regulated affiliate as well as the basis of each cost
25 allocation. In a convoluted response, Cindy Liles, CPA, Chief Financial Officer and Senior
26 Vice President of GWM, stated: "There are no "shared" or "common" services as AWC
27
28

1 uses the term.” At the same time, however, Global was stating in their response to Staff
2
3 Data Request LJ 1.1 (Exhibit JDH-4): “For instance, an integrated utility employs the same
4 Customer Service Representatives whether the call be about a sewer account or a water
5 account. Similarly, the number of Operations Staff is decreased as staff are cross-trained in
6 systems and can respond to issues on both water and wastewater. The list of combined
7 services that result in direct economies to the customers goes on.” (emphasis added)
8

9 Global’s list may go on but apparently Global cannot provide the factual data to
10 support such claims. The undisclosed methodology and resulting charges for personal
11 services provided by employees of other non-regulated Global affiliates is another source of
12 Global’s inefficiency.
13
14

15 **Q. DO YOU KNOW OF ANY OTHER REGULATED ARIZONA WATER OR**
16 **SEWER UTILITY THAT OPERATES WITHOUT ANY EMPLOYEES?**
17

18 A. Yes, those owned by AWRA, such as Black Mountain Sewer Company (“BMSC”),
19 Litchfield Park Service Company and several other regulated Arizona utilities controlled by
20 AWRA.
21

22
23 **Q. HAS THE COMMISSION ISSUED A RATE DECISION THAT DISCUSSED**
24 **THIS MANNER OF OPERATING A UTILITY WITHOUT ANY EMPLOYEES?**
25

26 A. Yes, in a recent BMSC rate case, (Decision No. 69164, December 5, 2006), the
27 Commission considered the way AWRA and BMSC are operated without employees and
28

1 stated: "AWRA, BMSC's sole shareholder has no employees. BMSC, as well as all of the
2 other regulated utility companies...have no employees. Instead, almost all operational
3 services are provided by an allegedly unregulated affiliate called Algonquin Water Services
4 ("AWS") that has between 70 and 90 employees and which, apparently, provides similar
5 services received by the regulated public service corporations owned by Algonquin in
6 Arizona, including BMSC."
7

8
9 Evidently there was a written contract between BMSC and AWS for provision of
10 wastewater services but it was not negotiated, and as recognized in the Decision: "BMSC
11 has in effect turned over the entirety of its operations and management to an (allegedly)
12 unregulated affiliate, and that the affiliate's shareholders have imposed a contract on
13 BMSC, without negotiation, that provides the affiliate with guaranteed profits at the expense
14 of BMSC's captive ratepayers."
15

16
17 Staff testimony cited in the Decision included one example of a billing rate of \$150
18 per hour for a "general manager" being charged to BMSC by its affiliate. Staff stated that
19 this rate equates to \$312,000 on an annual basis to perform management duties for BMSC
20 and contended that only the reasonable **actual** costs should be recovered from customers.
21 In Global's case there is no evidence of even a contract under which it imposes its charges
22 on its regulated subsidiaries.
23

24
25 **Q. DO THE PROBLEMS AND CONCERNS IDENTIFIED IN THE BMSC**
26 **DECISION APPLY TO THE GLOBAL ENTITIES?**
27
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1
2 A. Yes, they do. AWRA and Global share many similarities. They are the only two
3 entities operating Arizona regulated utilities without any employees. Global structured
4 itself and its utility model along the lines of AWRA, the first entity in the state with this
5 concept, and not surprisingly, several of Global's owners were former employees of AWRA
6 before forming Global.
7

8
9 **Q. WHAT ARE THE IMPLICATIONS IF GLOBAL IS ALLOWED TO**
10 **CONTINUE ITS RAPID EXPANSION BASED ON ITS HIGHLY QUESTIONABLE**
11 **SERVICE MODEL?**
12

13 A. The Decision in the BMSC rate case recognized the failings of this service model,
14 which adds additional layers of affiliate profit to the regulated utility's capital and operating
15 expenses. The Staff reply brief in the BMSC case concluded: "The Commission should
16 disallow affiliated profits even if the Company's business model achieves economies of
17 scale."
18

19 It was difficult and time intensive for Staff to untangle the web of hidden affiliate
20 charges in order to compute how much affiliate profit was actually included in the BMSC's
21 operating expenses and according to Staff, "...there may be additional affiliate profit that it
22 was unable to specifically identify."
23

24 However, those specific capitalized and expensed amounts that Staff was able to
25 determine were disallowed by the Decision, which provided: "We also share the concern
26 raised by staff that there may be additional affiliated profit margins built into the affiliate
27
28

1 billings that have not been specifically identified. Because we do not have any specific
2 record evidence of additional inappropriate profits in this case, we will exclude only the
3 “profits” that have been clearly identified by Staff. In doing so, however, we make no
4 finding as to the reasonableness of the Algonquin affiliate structure and, in future cases
5 involving the Algonquin companies, we expect all affiliate salaries, expenses, and billings
6 to be scrutinized to avoid potential abuses.”
7
8

9 As I explained, Global has refused to provide information about the way it also
10 imposes inter-company charges and clearly evaded having these charges scrutinized for
11 abuse. Accordingly, Global should be prohibited from expanding its operations into
12 enlarged CCN areas under its current organizational structure and operating model that
13 obscures the extent of its affiliates’ profits included in the regulated utilities rate bases and
14 operating expenses.
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18 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

19 **A.** Yes, it does.
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EXHIBITS

- JDH-1: Global's Expectation of ICFA Fee Revenues
- JDH-2: Global's Organizational Chart
- JDH-3: Arizona Water Company's Data Request 1.93
- JDH-4: Global's Response to Staff's Data Request LJ 1.1

ORIGINAL and 13 COPIES of the foregoing
filed this 3rd day of August, 2007 with:

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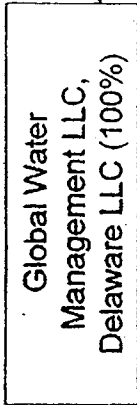
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JDH - 1

Builder/Owner	Date Executed	Rec. Number	GW Contact Person	Contact from Landowner/Developer via	Approx. Units	Anticipated Fees
Southeast Expansion						
Langley Properties (Talia West)	12/28/2005	*	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	1,509	\$5,432,400
Langley Stanfield Estates (Hay Hollow)	12/28/2005	2006-022209	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	1,544	5,558,400
Langley Properties (south part of JV with Wolfswinkle)	*	*	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	2,951	10,623,600
Langley Properties (Stanmar 160)	12/28/2005	2006-022208	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	560	2,016,000
Langley Properties (CCB Standfield Estates)	12/28/2005	2006-022207	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	336	1,209,600
Carranza Associates / Turner Dunn	12/28/2005	2006-022169	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	280	1,008,000
Stanfield Estates / Turner Dunn	12/28/2005	2006-022196	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	334	1,202,400
Dart Property / Terry Button	12/28/2005	2006-022197	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	2,170	7,812,000
Santa Cruz Land Co / Santa Cruz Ranch / Anderson Val Vista 6	12/28/2005	2006-022198	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	4,157	14,965,200
SCR, LLC / Scott Cole & Bryan Hartman	12/28/2005	2006-022199	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	2,359	8,492,400
El Dorado: Big Trail, LLC / Dunmar Farms / B Bennett	*	*	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	2,240	8,064,000
El Dorado: Lonely Trail 780	*	*	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	2,730	9,828,000
El Dorado: Parker Estates	12/28/2005	2006-022206	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	2,240	8,064,000
El Dorado: Hondo 640	12/28/2005	2006-022170	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	2,240	8,064,000
El Dorado: Rio Lobo, LLC	12/28/2005	2006-022174	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	2,240	8,064,000
JP Holdings LP / Solana Ranch North	12/28/2005	2006-022191	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	2,335	8,406,000
Anderson & Barnes 580 LLP / Solana Ranch South	12/28/2005	2006-022193	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	2,030	7,308,000
120 Townsend (Yount)	12/28/2005	2006-022187	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	700	2,520,000
NS120 (Yount)	12/28/2005	2006-022175	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	420	1,512,000
Montgomery 155 (Yount)	12/28/2005	2006-022179	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	546	1,965,600
CG 215 (Yount)	12/28/2005	2006-022188	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	753	2,710,800
Casa Grande Montgomery 240 (Yount)	12/28/2005	2006-022177	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	840	3,024,000
RRY Casa Grande 320 (Yount)	12/28/2005	2006-022180	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	1,120	4,032,000
SVVM 80 (Yount)	12/28/2005	2006-022181	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	280	1,008,000
VV Monty (Yount)	12/28/2005	2006-022176	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	210	756,000
RRY Real Estate (Yount)	12/28/2005	2006-022182	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	140	504,000
Robin R Yount LTD (Yount)	12/28/2005	2006-022189	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	140	504,000
Richard and Dana (Yount)	12/28/2005	2006-022186	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	140	504,000
Bruce and Karen (Yount)	12/28/2005	2006-022185	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	140	504,000
Sacaton BL (Yount)	12/28/2005	2006-022178	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	980	3,528,000
Trading Post Road LLC (Yount)	12/28/2005	2006-022183	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	210	756,000
Chartwell Casa Grande (Yount)	12/28/2005	2006-022184	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	140	504,000
Polich - Non Pulte	12/28/2005	2006-022194	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	4,256	15,321,600
Polich - Pulte	12/28/2005	2006-022192	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	5,194	18,698,400
ROB-LIN Marketing (Vistoso)	*	*	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	4,298	15,472,800
Vistoso Partners / Jorde Hacienda	*	*	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	10,920	39,312,000
ABCDW, LLC (Vistoso Stanfield 1942)	*	*	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	6,797	24,469,200
Vanderbilt Farms, LLC (Thude/Vistoso)	*	*	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	6,720	24,192,000
CRW Holdings, LLC (Mark Williams)	12/28/2005	2006-022203	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	105	378,000
Val Vista & Montgomery (Mark Williams)	12/28/2005	2006-022202	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	140	504,000
Williams Trusts (Mark Williams)	12/28/2005	2006-022173	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	560	2,016,000
Blevins	12/28/2005	2006-022201	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	560	2,016,000
Terbus Investments	12/28/2005	2006-022172	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	140	504,000
Douglas Payne	12/28/2005	2006-022171	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	280	1,008,000
Kronwald Family Trust	12/28/2005	2006-022205	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	280	1,008,000
Teel 80	12/28/2005	2006-022195	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	287	1,033,200
Mat Montgomery/SPD, INC	*	*	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	4,200	15,120,000
Ken Lowman	12/28/2005	2006-022204	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	280	1,008,000
Tim Nyberg / Hampden and Chambers	12/28/2005	2006-022190	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	2,825	10,170,000
Henry McMillan and Alexander McMillan	12/28/2005	2006-022200	Cindy Liles and/or Jennie Critchfield	Telephone, Email and/or In-house meetings	88	316,800
Southeast Expansion					86,944	\$312,998,400

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**ARIZONA WATER COMPANY'S
FIRST SET OF DATA REQUESTS
TO SANTA CRUZ WATER COMPANY
AND PALO VERDE UTILITIES COMPANY**

Docket No. W-01445A-06-0199

October 3, 2006

- AWC 1.1 Identify all property owners contacted in any way (personal visit, mail, correspondence, email, telephone, advertisement or other communication calculated to elicit a response) by Santa Cruz Water Company ("SCWC"), Palo Verde Utilities Company ("PVUC"), Global Water Resources, LLC, Global Water Resources, Inc., and any company, entity, or person affiliated with, employed by, or acting on behalf of the foregoing entities (collectively, the "Global Entities") to discuss that property owner's entry into an Infrastructure Coordination and Financing Agreement ("ICFA") or similar agreement.
- AWC 1.2 For each property owner identified in response to AWC 1.1, identify the date of communication, manner of communication (written or oral) and the name and title of the person who made the contact.
- AWC 1.3 For each property owner identified in response to AWC 1.1, provide copies of all written correspondence and documents of any nature (draft or final) provided to or received from the property owner concerning the ICFA.
- AWC 1.4 For each property owner identified in response to AWC 1.1, describe in detail all oral communications and provide copies of all written communications, including but not limited to representations or promises, made to the property owner concerning the ICFA.
- AWC 1.5 Provide copies of all ICFA's which have been proposed to or entered into with a property owner, whether in draft or final form, executed or unexecuted, and for each, disclose whether it is recorded in the State of Arizona, and if so, provide the recording information.
- AWC 1.6 Provide an updated map or maps showing all areas in the State of Arizona which any of the Global Entities believes or asserts are subject to an ICFA.
- AWC 1.7 For each property owner identified in response to AWC 1.1, provide an accounting of all monies or other consideration received or to be received by any of the Global Entities under or related to any ICFA.
- AWC 1.8 Identify all municipalities, counties or other governmental or quasi-governmental entities contacted in any way (personal visit, mail,

- AWC 1.85 List all sources of non-CAP surface water of SCWC, PVUC and each of the Global Entities and provide the quantity of each source available for 2007-2011, by year.
- AWC 1.86 Provide a copy of the regional plan "supported by Pinal County, the City of Maricopa and the City of Casa Grande" referred to in the April 6, 2006 response to Staff's insufficiency letter dated February 8, 2006.
- AWC 1.87 Provide a list of each regulated water affiliates' current employees showing, for each employee, the employee's job title, year hired by affiliate, years of experience with other water utilities, certifications by level, degrees, professional certifications and state licenses.
- AWC 1.88 Provide the authorized return on rate base for each regulated affiliate, including the Docket Number, Decision and date the return was authorized.
- AWC 1.89 List any regulated water affiliate that earned more than its authorized return in any of the last three calendar years, and for each such affiliate, if any, provide the amount and percentage of such earning by year.
- AWC 1.90 For each regulated affiliate, provide the operating income, calculated rate base and realized return for each of the last three calendar years.
- AWC 1.91 Provide an itemized description and calculation of the amounts of the annual savings each of the regulated Global Entities have realized by operating as an integrated water and sewer provider for each of the last three years.
- AWC 1.92 Provide a copy of all inter-company agreements between SCWC, PVUC and any of the Global Entities covering the provision of integrated services between regulated affiliates, including existing common or shared services (such as any type of management services, financing, employee sharing), and cooperative maintenance or operations agreements, that enable greater efficiency and cost savings to the integrated regulated utilities, and provide the Decision number and a copy of the relevant portion of the Decision authorizing the shared service and accounting requirements.
- AWC 1.93 For each of the last three years, provide the total costs of each common or shared service referred to in AWC 1.92 or AWC 1.93 above. For each common or shared service provide the amount and percentage of total costs allocated to each regulated affiliate and the basis of each cost allocation.

- AWC 1.94 Identify the source of water supply and storage that SCWC, its affiliates or holding companies will use to meet the water demands in the area that SCWC is seeking to add to its certificated area in this case.
- AWC 1.95 Provide copies of all approvals to construct a water system that SCWC or any of the Global Entities has received from the Arizona Department of Environmental Quality to serve, or help to serve the area that SCWC is seeking to add to its certificated area in this case.
- AWC 1.96 What is estimated cost of all facilities currently believed necessary for arsenic treatment and removal in the area that SCWC seeks to add to its certificated area in this case?
- AWC 1.97 Is the estimated cost in AWC 1.96, above, reflected in SCWC's proposed rates for serving the area it seeks to add to its certificated area in this case? If not, what impact does SCWC estimate that estimated cost will have on SCWC's proposed rates?
- AWC1.98 Summarize all plans by SCWC or any of the Global Entities for the treatment and removal of arsenic from the water SCWC plans to serve the area that SCWC seeks to add to its certificated area in this case.
- AWC 1.99 Provide a current list of regulated water or wastewater utilities owned in whole or in part by any of the Global Entities, and provide a current CCN map for each entity.
- AWC 1.100 For any ownership interest identified in response to AWC 1.99 that was originally acquired or increased in the last five years, include without limitation the type of each acquisition, the date and description of each individual transaction, the purchaser, the amount paid, and the percentage of entity owned as of October 1, 2006. Please describe the source of funds for each acquisition and provide a descriptive copy of all journal entries related to each purchase.
- AWC 1.101 For each ICFA, list the payments that have been received by date and the remaining estimated payments that are required. Describe the accounting for ICFA payments, all specific limitations on the use of ICFA funds, permissible uses and the amount expended, disbursed or invested by year, type of use and receiving payee/affiliate. Provide the descriptive journal entries used by any affiliate to record payment or any transfers of ICFA funds to the affiliate.
- AWC 1.102 Provide a descriptive list of all capital transactions including the date and amount for the last 5 years between all Global Entities not previously described in response to AWC 1.100.

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PALO VERDE UTILITIES COMPANY
AND SANTA CRUZ WATER COMPANY
RESPONSES TO STAFF'S 1ST SET OF DATA REQUESTS
DOCKET NO. W-01445A-06-0199, SW-03575A-05-0926
& W-03576A-05-0926
SEPTEMBER 25, 2006

LJ 1.1 Provide any study or analysis performed by Santa Cruz, Palo Verde or any public utility, public utility affiliate or public utility research firm which estimates costs savings to ratepayers who are provided water and wastewater services by affiliates compared to water and wastewater services provided by non-affiliates.

Response:

This is a matter of fact. The simple act of combining services under one umbrella will result in economies of scale and scope that non-affiliates cannot achieve. There is substantial economic literature on these concepts. One example that applies directly to the Arizona Corporation Commission ("ACC") is described below.

In June of 2002, the National Regulatory Research Institute provided the ACC with "NRRI Training for the Staff of the Arizona Corporation Commission" that addressed the issues Staff raises. Some highlights include:

- "Service Incremental Cost ('SIC') is estimated by determining the change in total costs resulting from adding an entire service (or the costs saved by dropping it)"
- "Long-run cost calculations assume that all inputs are variable so that plant and equipment may be optimized. There are no fixed costs in the long run."
- "Total Service Long Run Incremental Cost ('TSLRIC') is a form of service incremental cost calculation that estimates the cost of adding a whole service to a network that's already providing a range of other services. The 'long run' implies that the network can be optimized to deliver the new mix of services at least cost"
- "TSLRIC includes the fixed costs associated with adding a service"
- "Economies of scale mean that a firm's average cost decreases as its output rises...Note: If economies of scale exist over the range of output up to the level of market demand, the industry is a natural monopoly – the market demand can be met by one firm at a lower total cost than it can be met by two or more firms."
- **"If a firm has economies of scope, it can jointly produce multiple outputs for less than it – or several independent firms – could produce them on a stand-alone basis."** [emphasis added]
- "Economies of scope can arise because outputs may have shared or common costs or because the products are linked vertically, so that it is cheaper for a single firm to coordinate production."
- **"In multi-product firms with economies of scope, it becomes difficult to talk unambiguously about the 'cost' of a single product."** [emphasis added]

PALO VERDE UTILITIES COMPANY
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RESPONSES TO STAFF'S 1ST SET OF DATA REQUESTS
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The question may arise then, whether, if 'cost' is difficult to discuss, subsidization is occurring. Happily, the NRRI provided a simple test for that scenario:

- "So long as a service is paying at least its total incremental cost, it is not receiving a subsidy. One view of 'contribution' is that anything in excess of incremental cost may be viewed as contributing to joint and common or overhead costs. Contribution is often measured as the difference between the revenues obtained from a customer class or service and the customer class or service's direct embedded or accounting costs. This excess can be used to cover joint, common and overhead costs."

So clearly, there is positive value possible from integrated services, economies of scope and economies of scale. The ACC will note that in the last sentence of the preceding paragraph the question arises whether there is a negative impact possible from the integrated service scenario. NRRI addressed that question succinctly:

- "So long as revenues from a service or group of services is paying at least its incremental cost, the firm is no worse off for offering them.", but
- "[I]f it prices all services to recover only incremental cost, a firm with economies of scope cannot stay in business, because $SIC_1 + SIC_2 < C(Q_1, Q_2) < C(Q_1) + C(Q_2)$."

Global Water Resources, LLC ("Global") used these concepts in developing its integrated model of water, wastewater, and reclaimed water services for its regulated subsidiaries. Global's regulated subsidiaries use – wherever possible – the triad of conservation. The triad involves providing reclaimed water, surface water, and using recharge wells to dramatically reduce reliance on groundwater. The triad can only be provided by integrated utilities. While the triad is critical to groundwater conservation, it has another key advantage – it enables the utilities to achieve economies of scale and scope.

Concepts such as economies of scale and scope are not merely theoretical. Indeed, they are a critical part of Global's business model. Global's experience in operating integrated utilities which implement the triad of conservation demonstrates that there are many practical advantages to the integrated model. For instance, an integrated utility employs the same Customer Service Representatives whether the call be about a sewer account or a water account. Similarly, the number of Operations Staff is decreased as staff are cross-trained in systems and can respond to issues on both water and wastewater. The cost of the supply of consumables is also reduced as the ability to bulk-purchase for both utility services allows for reduced delivery fees. The list of combined services that result in direct economies to the customers goes on:

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- Cross trained operations and maintenance staff can significantly reduce the number of staff required for affiliated entities, compared to non-integrated utilities which must staff water and wastewater separately
- Operating costs can be reduced when buying in larger quantities or when combining usage, associated with affiliated services; for eg., chemicals, tools, warehousing, uniforms, power, laboratory analytical costs, etc.
- Blue-staking (an integrated utility can employ the same people to mark all underground services)
- Compliance (monitoring, analysis, reporting, inspection, enforcement (each utility must maintain its own compliance staff in a non-affiliated scenario)
- Accounting (two sets of accounting staff are required for non-integrated entities)
- Account set-up and maintenance (one account versus two)
- Account transfers (two accounts must be manipulated in a non-integrated utility)
- Billing and mailing (two invoices and two mailings are required per connection with a non-integrated service model, versus one with an integrated utility servicing approach)
- On-call services (a non-integrated utility requires twice the number of personnel on call)

In non-integrated utility, each of these elements is required to be staffed, administered and executed separately. These additional costs will be reflected in the rates paid the ratepayers of non-integrated utilities.

This is not the first time that Staff has considered the economic benefits of integrated utilities. For example, in the Woodruff case, Staff stated that:

[T]he Woodruff Companies will be able to achieve economies of scale by sharing resources. For example, they may be able to share employees, equipment, and offices space. For this reason, [Assistant Director] Olea testified that "Staff supports regional planning for water and wastewater to ensure an economy of scale for **both** services."¹

Staff also remarked that by sharing financial resources, integrated utilities have "enhanced financial viability" compared to non-integrated utilities.²

In summary, substantial economic literature, Global's own practical experience, and Staff's previous analysis all support the conclusion that there are real and substantial

¹ Staff Brief in Docket No. W-01445A-04-0755, filed September 19, 2005 at 2-3.

² *Id.*

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economic benefits to ratepayers who receive service from integrated utilities. In addition, integrated utilities can provide the triad of conservation – and groundwater conservation is critical to the future of our state.

Respondent: Trevor T. Hill
President
Global Water Resources, LLC
21410 North 19th Avenue, Suite 201
Phoenix, Arizona 85027